



[6705-01-P]

FARM CREDIT ADMINISTRATION

12 CFR Part 612

RIN 3052-AC44

Standards of Conduct and Referral of Known or Suspected Criminal Violations; Standards of Conduct

AGENCY: Farm Credit Administration.

ACTION: Proposed rule.

SUMMARY: The Farm Credit Administration (FCA, we, or our) proposes to amend its regulations governing standards of conduct of directors, employees, and agents of Farm Credit System (System) institutions, excluding the Federal Agricultural Mortgage Corporation. The amendments would clarify and strengthen reporting requirements and prohibitions, require institutions to establish a Code of Ethics, and enhance the role of the Standards of Conduct Official.

DATES: You may send comments on or before [Insert date 90 days after publication in the Federal Register].

ADDRESSES: We offer a variety of methods for you to submit your comments. For accuracy and efficiency reasons, commenters are encouraged to submit comments by e-mail or through the FCA's Web site. As facsimiles (fax) are

difficult for us to process and achieve compliance with section 508 of the Rehabilitation Act, we are no longer accepting comments submitted by fax. Regardless of the method you use, please do not submit your comment multiple times via different methods. You may submit comments by any of the following methods:

- E-mail: Send us an e-mail at reg-comm@fca.gov.
- FCA Web site: <http://www.fca.gov>. Select "Public Commenters," then "Public Comments" and follow the directions for "Submitting a Comment."
- Federal eRulemaking Portal: <http://www.regulations.gov>. Follow the instructions for submitting comments.
- Mail: Barry F. Mardock, Deputy Director, Office of Regulatory Policy, Farm Credit Administration, 1501 Farm Credit Drive, McLean, Virginia 22102-5090.

You may review copies of comments we receive at our office in McLean, Virginia, or from our Web site at <http://www.fca.gov>. Once you are in the Web site, select "Public Commenters," then "Public Comments" and follow the directions for "Reading Submitted Public Comments." We will show your comments as submitted but, for technical reasons, we may omit items such as logos and special

characters. Identifying information that you provide, such as phone numbers and addresses, will be publicly available. However, we will attempt to remove e-mail addresses to help reduce Internet spam.

FOR FURTHER INFORMATION CONTACT:

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SUPPLEMENTARY INFORMATION:

I. Objectives

The objectives of this proposed rule are to:

- Clarify and strengthen the regulations in part 612, subpart A, regarding standards of conduct;
- Modify definitions;
- Clarify reporting requirements and prohibitions on the purchase of System institution acquired property and lending transactions;
- Strengthen responsibility and accountability requirements for System institution Standards of Conduct Officials, boards of directors (or board), employees, and agents; and

- Require each System institution to adopt a Code of Ethics.

The FCA has not made significant changes to its standards of conduct regulations since 1994, and we have determined that it is appropriate to strengthen and modernize the rule. The proposed rule would add new provisions, clarify and augment some of the current provisions and provide additional flexibility for others. The proposed rule is organized differently from the current rule. Sections on director and employee reporting and prohibited conduct are repositioned to improve the logical flow of the rule. The proposed rule adds a new § 612.2136 on conflicts of interest, a new § 612.2165(a) on Code of Ethics, a new § 612.2165(c) on allowing exceptions to certain rules if no conflict of interest exists, and new requirements in § 612.2180 addressing standards of conduct for agents. It also adds new standards of conduct responsibilities to System institutions (proposed § 612.2160) and to the Standards of Conduct Official (proposed § 612.2170). We solicit comments on our proposed amendments.

II. Section-by-Section Analysis

A. Definitions [§ 612.2130]

The proposed rule would have some new and some modified definitions:

Code of Ethics. The proposed rule would define "Code of Ethics" as a written set of standards, rules, values, and guidance that an institution uses to ensure the ethical conduct of those who sign it, and that reflects professionalism and discourages misconduct so the best interests of the institution are advanced.

Controlled entity and entity controlled by. The proposed rule would continue to provide that a controlled entity includes an interest in an entity in which the individual, directly or indirectly or acting through or in concert with one or more persons, owns 5 percent or more of the equity of the entity; owns, controls, or has the power to vote 5 percent or more of any class of voting securities of the entity; or has the power to exercise a controlling influence over the management of the entity. The FCA is aware that in other contexts the definition of "controlled entity" or "entity controlled by" may mean having an ownership interest with a greater threshold than 5 percent; however, the purpose of this rule is to ensure that institution directors and employees are completely objective in their decision-making, and are not in any way influenced by personal interests. The FCA believes that a reasonable person could conclude that a director or employee could be influenced to act favorably toward an

entity in which he or she had an economic interest of 5 percent or more. Therefore, directors and employees should report these interests and should abstain from decision-making with regard to them. So, for the purpose of this rule only, a "controlled entity" or "entity controlled by" is defined as an entity in which the director or employee has an interest of 5 percent or more, alone or in concert with others, directly or indirectly.

Employee. The proposed rule would clarify the definition of "employee" to include non-salaried employees such as hourly wage earners.

Entity. The proposed rule would add unincorporated business entities to the definition of "entity".

Family. The proposed rule would add to the current definition of "family" associations or relationships that are in the nature of a family relationship. This is intended to modernize the definition of family to include non-traditional relationships, and adoptions and other relationships where an adult who is not related to a child acts as a parent to a child living in the home. Each System institution is encouraged to provide more explanation and discussion of the regulatory definition in its standards of conduct policies and procedures.

Material. The proposed rule would not change the definition of "material." However, each System institution must set specific parameters on what constitutes a material financial interest or transaction. The value of a material financial interest or transaction may change depending on the circumstances and, to some extent, the geographic location of the institution involved. The institution's determination of materiality would be subject to FCA examination.

The institution's policies and procedures may include de minimis values below which a financial interest is determined by the board not to be material. The de minimis amount is necessarily System institution-specific, and must be appropriate to the institution's size, location and risk tolerance. A de minimis amount is an amount or value representing an interest that is so insignificant that no reasonable person could conclude that it would influence a director or employee's ability to act impartially and in the best interests of the System institution. The institution would need to adequately support the values established in its determination of de minimis or not material, and this determination would be subject to FCA examination.

Officer. We propose to replace "secretary" with corporate secretary.

Ordinary course of business. We propose to remove "two" concerning transactions between persons and add "agents" to those for whom preferential treatment should be avoided.

Signed. We would add a definition of "signed" to have the same meaning as set forth in § 620.1 of the chapter, to provide for greater uniformity in our regulations and to clarify electronic signatures are acceptable.

Unincorporated business entities. We would add a definition of "unincorporated business entities" to have the same meaning as set forth in § 611.1151 of the chapter.

B. Director and Employee Responsibilities and Conduct--
Generally [proposed § 612.2135]

The section heading would be replaced with "responsibilities and conduct" but otherwise this section is not substantively changed. The words "and guidance" are added to paragraph (b) to make clear that in addition to regulations, policy statements, instructions and procedures, directors and employees must observe guidance of the FCA, to the best of their abilities.

C. Conflicts of Interest [proposed § 612.2136]

The proposed rule would add a new § 612.2136 on conflicts of interest. This section is added to require directors, employees, and agents to take affirmative action to report conflicts of which they are aware. It is intended to compel them to take ownership of and invest in their ethical responsibilities. Paragraph (a) would specifically require directors, employees, and agents to disclose any conflicts of interests they may have in any matters, activities or transactions pending at the System institution to the Standards of Conduct Official. It would require immediate reporting of conflicts of interests and would supplement employee's and director's existing annual and periodic reporting requirements. Paragraph (b) would require recusal from any board action on, discussion of, or any other official action on or discussion of, those matters. For example, if a director or employee were to purchase farm equipment such as a combine harvester from a known borrower, the purchase should be reported and reviewed by the Standards of Conduct Official for conflicts. If the borrower has a matter or transaction pending at the institution, the director or employee would be recused from that matter. Note that if the purchase were financed it would be a lending transaction covered by §§ 612.2145 and 612.2155. Working together with other

provisions of the rule, this section is intended to bolster the directors', employees', and agents' loyalty to the System institution and to reinforce personal responsibility and accountability in avoiding conflicts and acting ethically.

The requirements of disclosure and recusal in this section apply not only to directors, employees, and agents, but also those consultants, professionals or experts who are hired to give advice on a matter, transaction or activity but may not necessarily meet our definition of "agent". If the consultant, professional or expert has an interest that may compromise his or her complete impartiality in a matter, transaction or activity for which his or her expertise is sought, paragraph (a) requires that he or she disclose that interest and paragraph (b) requires that he or she refrain from further discussion of System business with respect to that matter, transaction or activity.

System institutions must develop policies and procedures to implement this section. Such policies and procedures could include procedures for waiver of the recusal requirement if the Standards of Conduct Official determines in writing that the conflict would not interfere with the person's ability to perform impartially and in the

best interest of the System institution. In the absence of such waiver procedures, recusal is required.

D. Director Reporting [current § 612.2145 is proposed § 612.2140]

We would revise § 612.2140(b)(1) to require that each director report all "material" financial interests with other directors, employees, agents or borrowers of the employing, supervised, and supervising institution. We believe this section is necessary to help directors and Standards of Conduct Officials identify and avoid potential conflicts of interests. Because the proposed rule would require directors to report only material financial interests we believe the requirement will not be unduly burdensome or intrusive.

As discussed in the section-by-section analysis above, each System institution must develop policies and procedures that provide parameters for that which constitutes a "material" financial interest, and may develop policies and procedures that set forth a certain de minimis value that would not be considered material for reporting requirements. Reporting of material financial interests is intended to assist the Standards of Conduct Official in identifying and resolving conflict situations and to help a director identify areas of prohibited

conduct. A material financial interest does not necessarily mean that a conflict of interest exists or that the interest would unduly influence the director in his or her position.

Like the current rule, the proposed rule would require directors to report the name of any relative or person residing in the director's household, any business partner, or any entity controlled by the director or such persons (alone or in concert) if the director knows or has reason to know that such individual or entity transacts business with the institution or any institution supervised by the director's institution. This rule does not require a director to solicit information from these persons or entities to determine whether they had or have transactions with the institution. However, the FCA presumes that a director would know or have reason to know whether or not a relative or other persons residing in the director's household had or has transactions with the institution.

E. Directors--Prohibited Conduct [current § 612.2140 is proposed § 612.2145]

In our current rule, director prohibited conduct and the related limited exceptions are included in the same discussion. In proposed § 612.2145(a), we set forth the basic rules for prohibited conduct. In proposed

§ 612.2145(b), we set forth the specific limitations and exceptions to the prohibitions. We believe this change is necessary to remove any possible ambiguity from the meaning of the prohibitions. Most of these changes are straightforward, but proposed § 612.2145(a)(6) and (b)(3) regarding acquired property and proposed § 612.2145(a)(7) and (b)(4) regarding lending transactions require special discussion.

The proposed rule would clarify the circumstances under which directors may and may not purchase property that a System institution has owned or acquired by foreclosure or similar action. These proposed changes are not substantive; they are clarifications of the rule. Proposed § 612.2145(a)(6) would provide that, among other things, a director may not knowingly acquire, directly or indirectly, property that was owned or acquired by the employing, supervising or supervised institution as a result of foreclosure or similar action. Proposed § 612.2145(b)(3) would set forth an exception to the acquired property prohibition in proposed § 612.2145(a)(6). The exception would apply only if the director did not participate in the deliberations or decision to foreclose, or to take similar action, or to dispose of the property or in establishing the terms of the sale, and (1) the director

acquired the property through inheritance, or (2) the System institution did not own the property or an interest in the property at any time during the 12-month period before the director's acquisition of the property, or (3) the director acquired the property through public auction with open competitive bidding and the Standards of Conduct Official determined, before the director acquired the property, that the director does not have an advantage over other bidders as a result of the director's position and that no other conflict of interest or the appearance thereof exists.

By open competitive bidding, we mean bidding that is both competitive, allowing involvement of all interested parties, and that is open and unsealed. Open competitive bidding affords all interested parties an opportunity to counter-bid. The advantage to open bidding is that it discourages unethical behavior or favoritism. A public auction can be accomplished on-line as long as there is an opportunity for all who may be interested to bid.

The proposed language does not reflect a substantive change from the intent of this original regulatory provision regarding acquired property. However, we believe that because of the scope of misunderstanding and

misapplication of the original provision, the revision is necessary.

Proposed § 612.2145(a)(7) would provide that a director must not directly or indirectly borrow from, lend to, or become financially obligated with or on behalf of a director, employee, or agent of the employing, supervising or supervised institution or a borrower or loan applicant of the employing institution. This section addresses lending and borrowing relationships. It prohibits a director from entering into a lending or borrowing transaction with those who may have a financial relationship with the System institution. Lending and borrowing relationships include providing guarantees or stand-by letters of credit and similar forms of financial obligation.

The FCA recognizes that there are many situations in which a director may enter into lending transactions or business relationships that involve financing with other directors, employees, agents, borrowers or loan applicants in the ordinary course of business. Therefore, to keep the provision from being unduly restrictive, proposed § 612.2145(b)(4) would set forth an exception to the proposed § 612.2145(a)(7) prohibition. The exception would apply if: (1) The transaction is with a relative or any

person residing in the director's household; or (2) the transaction is undertaken in an official capacity in connection with the institution's discounting, lending or participation relationships with OFIs and other lenders; or (3) the Standards of Conduct Official determines, as authorized under board policy and in the manner outlined in the rule, that the potential for a conflict of interest is insignificant. The Standards of Conduct Official's determination must be in writing; document that the transaction is in the ordinary course of business or is not material in value or amount; document that the director did not participate in the determination of any matter affecting the financial interests of the other party to the transaction except those matters affecting all shareholders/borrowers in a nondiscriminatory way; and most importantly, the Standards of Conduct Official's determination be made before the director enters into the transaction. The Standards of Conduct Official must renew this determination annually, as applicable. For example, if a director and a borrower contemplate an ongoing business relationship by which the director purchases grain from a borrower on credit on a regular basis, the Standards of Conduct Official would have to review this relationship for conflicts. Once reviewed, to the extent this is an

ongoing relationship in the ordinary course of business, the Standards of Conduct Official would not have to review each and every transaction, but would renew on an annual basis his or her determination that the ongoing relationship remains in the ordinary course of business and does not create a conflict.

The Standards of Conduct Official cannot ratify prohibited conduct after the fact. If the transaction has been entered into without a pre-existing Standards of Conduct Official determination, then the FCA could consider the director to have violated this provision of the regulation.

As discussed, each System institution must set specific parameters on what constitutes a material financial interest or transaction and also what is in the ordinary course of business in the local environment. Whether or not to establish a de minimis threshold for review would be left to the discretion of each System institution board; however, as discussed above, if the institution does establish a de minimis value, it must do so under policies and procedures subject to FCA examination. The institution's board must not establish the de minimis value to be so high or so ambiguous as to circumvent the intent of this rule.

F. Employee Reporting [current § 612.2155 is proposed
§ 612.2150]

This provision would require employees to report all "material" financial interests with directors, employees, agents or borrowers of the employing, supervised, and supervising institution. This change can be found in proposed § 612.2150(b)(1) and is parallel to the change for directors in proposed § 612.2140(b)(1).

G. Employees--Prohibited Conduct [current § 612.2150 is
proposed § 612.2155]

This provision has been changed from the current § 612.2150 and the revisions are parallel to the changes for director prohibited conduct, where applicable.

H. Joint Employees [proposed § 612.2157]

This section, like the current rule, prohibits an officer of a Farm Credit Bank (FCB) or agricultural credit bank (ACB) from contemporaneously working as an employee at an association in its district. Also, this provision prohibits a non-officer employee of a FCB or ACB from serving as an officer of an association in its district. The FCA recognizes that occasionally the System may benefit from having a FCB or an ACB officer serve at an association. Therefore, this provision is modified from the original to allow joint employee relationships with the

written approval of the Standards of Conduct Official if the bank board of directors agrees that the interests of both System institutions outweighs the potential for conflicts of interest or conflicts related to devotion of time to official duties. The bank must provide written notice to the FCA before the joint relationship begins, and the FCA may object within 10 calendar days of receiving the bank's notice.

I. Institution Responsibilities [proposed § 612.2160]

The proposed rule would update this section to require new responsibilities and accountability of System institutions in overseeing the standards of conduct program.

Proposed § 612.2160(a)(1) would require the institution to dedicate appropriate resources to support the standards of conduct program. The Standards of Conduct Official has many duties and responsibilities, and depending on the size of the institution it may not be possible for one person to satisfactorily manage all of these responsibilities. Each System institution should dedicate personnel and resources as necessary to ensure that the standards of conduct program is carried out thoroughly and in compliance with this rule.

Proposed § 612.2160(a)(3) would require the institution to notify the FCA immediately of any known or suspected material standards of conduct violations. This notification can come directly from the board of directors, or from the Standards of Conduct Official as separately required in proposed § 612.2170(b)(7). The requirement is added here to make clear that the institution itself is accountable for notifying the FCA of known or suspected standards of conduct violations.

Proposed § 612.2160(e) would require the institution to ensure that directors and employees certify annually that they will adhere to the institution's standards of conduct policy and Code of Ethics. System institutions would be required under § 612.2160(f) to have documentation that agents (1) are subject to applicable industry or professional ethics standards, or (2) have certified to adhere to the provisions of the System institution's Code of Ethics applicable to agents. The certifications could be performed in various ways including electronic signatures.

Proposed § 612.2160(g) would require that System institutions make compliance with the standards of conduct program a component of the risk assessment process subject to periodic audit, as established by the audit committee,

by a person or entity independent of the standards of conduct program. We would expect an institution to audit the standards of conduct program at least once every 3 to 4 years consistent with its risk assessment and audit planning process. The scope and depth of the audit would be determined and documented by the institution.

Proposed § 612.2160(h) would require institutions to establish an effective method of internal controls over the reporting, disclosing, and other requirements of this part, including controls for the confidentiality of information reported to and maintained by the Standards of Conduct Official. It would require institutions to establish an effective method of internal controls over the audit of the standards of conduct program.

J. Code of Ethics, Policies and Procedures [proposed § 612.2165]

Many of the provisions in proposed § 612.2165 would be the same as the provisions in current § 612.2165. However, each institution should have a strong sense of its role in the System's mission and should have a culture of corporate and personal responsibility to further that mission.

Therefore, in addition to adopting internal standards of conduct policies and procedures, proposed § 612.2165(a) would require each System institution to adopt a Code of

Ethics that applies to directors and employees and that includes a provision for the ethical conduct of agents. Each institution would be required to provide a copy of its Code of Ethics to directors, employees, and agents. Directors and employees would be required to sign the institution's Code of Ethics. Agents not subject to industry or professional ethics standards would be required to certify that they will adhere to the institution's Code of Ethics provision applicable to agents.

The proposed rule sets forth minimum specific guidelines that each System institution's Code of Ethics would be required to meet. The institution's Code of Ethics must promote honest and ethical conduct including the ethical handling of actual or apparent conflicts of interest; promote integrity and compliance with laws and regulations; prohibit dishonesty, fraud or deceit and discourage any conduct or act that would adversely reflect on the reputation, integrity or competency of the System; prohibit misuse of office and provide for the prompt reporting of any person or persons who violates the institution's Code of Ethics or engages in any activity that may require further investigation under § 612.2301, subpart B of the part, to the Standards of Conduct Official.

Proposed § 612.2165(a)(3) would require each institution's board to adopt policies and procedures concerning the use of unincorporated business entities (UBEs) that, at a minimum, ensure that all transactions between the UBE and System institution directors, employees, and agents are conducted at arm's length. These policies and procedures must ensure that System institution directors, employees, and agents comply with their employing institution standards of conduct policies and procedures and this rule in their interactions with the UBE. For example, System institution directors, employees, and agents cannot purchase acquired property from a UBE except in compliance with this rule and their institution's standards of conduct policies and procedures.

The FCA believes that each System institution must review and update its standards of conduct policies and procedures, as necessary, to strengthen them. The FCA expects each System institution to modernize and augment its existing standards of conduct policies and procedures to ensure the highest standards of honesty, ethics, integrity, impartiality and conduct. In doing this, each System institution should establish reasonable criteria for business relationships and transactions relevant to its business, geographic location, and customer base. The

standards outlined in this rule serve as a minimum bar against which each System institution should build and develop stronger internal standards of conduct policies and procedures.

Proposed § 612.2165(b)(2) would require System institutions to outline authorities and responsibilities of the Standards of Conduct Official. Included in this requirement would be the authority and responsibility to review for compliance with this subpart all loans considered for approval by the supervisory bank under §§ 614.4460 and 614.4470, respectively. System institution loans to directors and employees and loans to FCA employees and others subject to §§ 614.4460 and 614.4470 present unique conflict of interest issues. The System institutions should ensure that credit decisions with respect to these loans are made without favoritism or special terms. These loans, which include insider loans, warrant a higher level of scrutiny for possible conflict or undue influence than non-insider loans.

Proposed § 612.2165(b)(14) would clarify the circumstances under which an institution's policies and procedures must prohibit the purchase and retirement of the institution's preferred stock. This section does not place a restriction on the issuance or retirement of borrower

stock associated with a director or employee loan transaction.

Proposed § 612.2165(b)(16) would require the board in its policies and procedures to provide for annual training on standards of conduct. Training presents an opportunity to continually educate directors and employees on standards of conduct issues and the importance of ethical behavior.

Proposed § 612.2165(b)(17) would require the institution to report to the FCA exceptions authorized by the institution board under § 612.2165(c).

The FCA recognizes that some of the provisions of the rule may prohibit activity where no actual or apparent conflict of interest exists. Therefore, proposed § 612.2165(c)(1) would allow each System institution to adopt policies and procedures by which the System institution board of directors may grant a written exception to certain standards of conduct rules under this subpart. The FCA proposes that rules for which an exception may be granted on a case-by-case basis are a reporting requirement, an employee or director prohibition on disclosure of information not generally available to the public, an employee prohibition on serving as an officer of a non-System entity in the district or of a non-System financial institution, a restriction on an employee serving

jointly at a bank and association as discussed in proposed § 612.2157, and the 5-percent threshold for defining a controlled entity. For example, under proposed § 612.2165(c)(1) a board could allow an exception to the prohibition with respect to an individual director's interest in a "controlled entity" where that director indirectly owns more than 5 percent of the equity and the Standards of Conduct Official determines based on the facts and circumstances that there is no potential for conflict of interest. As another example, this provision would allow the board to approve an exception to the prohibition on an employee serving as an officer or director of a non-System entity that transacts business with the System institution in its district (proposed § 612.2155(a)(4)), if the Standards of Conduct Official determines that there is no conflict of interest.

The exceptions under proposed § 612.2165(c)(1) would have to be approved on a case-by-case basis by the institution's board, based on a recommendation of the Standards of Conduct Official. The Standards of Conduct Official's recommendation would need to be strongly supported by a written determination that the prohibition is not necessary to avoid a conflict or appearance of a conflict or to ensure impartiality, objectivity and public

confidence in the System institution. The determination would have to be documented in the institution's files and renewed at least annually. The institution board would impose appropriate conditions, as the circumstances may dictate. In addition, the board would provide for periodic review of the criteria to determine whether the board continues to support the Standards of Conduct Official's recommendation. The exceptions approved would be subject to FCA examination, and to its determination of whether the prohibition of the activity is necessary to avoid a conflict or appearance of a conflict or to ensure impartiality, objectivity and public confidence in the System institution.

The FCA specifically requests comment on whether the provisions proposed are appropriate for board waiver and whether other provisions should be considered. There are some transactions so susceptible to conflicts that the FCA would not consider permitting a waiver of the rule prohibiting them. The rules prohibiting directors, employees, and agents from acquiring property could not be waived. The rules prohibiting an employee from acting as a real estate agent or broker could not be waived, and the rule prohibiting an employee from acting as an agent or broker in connection with the sale and placement of

insurance could not be waived. Finally the requirement to comply with the institution's standards of conduct policies and Code of Ethics could not be waived. As previously stated, there may be other rules for which an institution board may appropriately consider granting a waiver, and the FCA specifically requests comment on the waiver provisions of this proposal and what those rules may be.

Proposed paragraph (c)(2) of this section would allow the institution board to consider a standing exception to director and employee reporting requirements under proposed §§ 612.2140 and 612.2150, respectively. As an example, policies and procedures under proposed § 612.2165(c)(2) could allow an exception to the requirement that a director report the name and nature of a business or any entity on whose board the director sits, if the entity is a nonprofit organization such as a Chamber of Commerce, or a place of worship, and the Standards of Conduct Official determines that the potential for conflict is insignificant with respect to that category of entity.

Proposed paragraph (c)(2) would also permit the board to establish policies and procedures that provide for a standing exception to the restrictions in proposed §§ 612.2145(b)(4) and 612.2155(b)(6) on lending transactions, if the potential for conflict is

insignificant because the transaction is not material, or it is in the ordinary course of business. An institution may identify certain lending transactions that fall under a certain dollar value and are de minimis or immaterial. Those transactions falling below such identified amounts would not have to be reported to or reviewed by the Standards of Conduct Official. In addition, an institution may identify certain types of transactions that are in the ordinary course of business. Directors and employees could enter into those ordinary course of business transactions without the prior review of the Standards of Conduct Official. However, where the ordinary course of business transaction exceeds the de minimis or immaterial threshold set by the institution, the directors and employees must report such transactions, by including them in regular reports to the Standards of Conduct Official, and the Standards of Conduct Official must review them. Putting the exceptions of proposed § 612.2165(c)(2) together, a transaction that is in the ordinary course of business and that also is de minimis or falls below the immaterial amount would require neither director or employee reporting nor Standards of Conduct Official review.

For example, the System institution may find that certain goods and services that are offered to the public

in the ordinary course of business at a fixed price, such as diesel fuel, or equipment repairs, do not raise conflict of interest concerns, even if purchased from a System borrower with credit. Institution policies and procedures could provide that these transactions would not have to be reported or approved unless they reached a certain dollar amount or value threshold. By contrast, transactions involving price negotiation, such as purchasing a tractor or other heavy farm equipment, could raise issues of impartiality or favoritism and should be subject to more scrutiny.

In addition to transactions covered in the institution's policies and procedures under proposed § 612.2165(c)(2), proposed §§ 612.2145 and 612.2155 retain the existing flexibility for an institution's Standards of Conduct Official to review a transaction before it is entered into and make a case-by-case determination that there is no conflict. The exceptions in proposed § 612.2165(c)(2) are designed to be applied to all directors and employees and as such, must be set on a conservative basis. However, a particular lending transaction that does not fall within the institutions' § 612.2165(c)(2) exceptions may still be a transaction that the Standards of Conduct Official determines has little

potential for conflict when applying the rules under §§ 612.2145 and 612.2155. Proposed § 612.2165(f) reminds each System institution that the FCA may determine that a transaction or activity constitutes a conflict of interest notwithstanding the System institution's board of director finding to the contrary. Section 612.2165(d) and (e) are included to prevent misuse of the requirements under this section to evade conflict of interest rules and situations. Finally, institution policies and procedures should provide for periodic review by the System institution board.

K. Standards of Conduct Official [proposed § 612.2170]

We would revise § 612.2170(a) to require that there must be an internal employee who also serves as the institution's Standards of Conduct Official and who would be accountable to the institution's board for all standards of conduct matters. The FCA believes that an in-house Standards of Conduct Official is in the best position to advise the board because they are in-tune with the day-to-day operations of the institution. In addition, in order to foster a culture of highest integrity and ethical conduct, it is important to have a Standards of Conduct Official who has a constant presence at, relationship with, and respect of, the employees of the institution. The proposed rule would require the institution's board of

directors to provide for other employees to assist the Standards of Conduct Official as needed to ensure the effective operations of the institution's standards of conduct program.

Proposed § 612.2170(b) would enhance and clarify the responsibility and accountability of the Standards of Conduct Official. The Standards of Conduct Official must receive, actively review, and maintain the reports required by the rule. Proposed § 612.2170(b)(6) would require the Standards of Conduct Official to report to the board no less than annually on the effectiveness of the institution's standards of conduct policy and its implementation. This report should include an evaluation of the extent to which safeguards are in place to avoid conflicts of interest and standards of conduct policy violations and should present the opportunity to make improvements to the standards of conduct program.

The Standards of Conduct Official must also present any violations of the standards of conduct policy to the board for appropriate action. Section 612.2170(b)(7) would requires the Standards of Conduct Official to report to the institution's board and to the FCA all suspected criminal and, in addition, any standards of conduct violations that

may have an adverse impact on continued public confidence in the System or any of its institutions.

Proposed § 612.2170(c) would provide that a Farm Credit bank may provide assistance to an affiliated association's board of directors and Standards of Conduct Official in complying with this part. Proposed § 612.2170(d) would provide that an institution may use an outside counsel or consultant to assist the institution in meeting standards of conduct requirements. However, the institution's in-house Standards of Conduct Official would be responsible for overseeing the outside counsel or consultant.

Proposed § 612.2170(e) would provide that the Standards of Conduct Official must coordinate appropriate training with the institution's board on an annual basis.

L. Standards of Conduct for Agents [current § 612.2260 is proposed § 612.2180]

It is important for System institutions to hold their agents to the same high ethical standards held by their directors and employees. The proposed rule would require that institutions document that agents representing System institutions in contacts with third parties or who provide professional or consultant services such as legal, accounting, and appraisal, are subject to industry or

professional ethics standards and that the institution provide each agent a copy of the institution's standards of conduct policy and Code of Ethics. The proposed rule would further require that an agent who is not subject to industry or professional ethics standards must certify to the System institution that the agent will adhere to the provisions of the institution's Code of Ethics applicable to agents. Agents play an important role in System institutions and this rule would help achieve high ethical standards at every level throughout the System.

To avoid the appearance of conflicts in the disposition or purchase of institution-owned or institution-acquired real or personal property, we propose that agents must agree to prohibitions similar to those that apply to employees. The proposed rule would prohibit agents from acquiring any interest in real or personal property if it was owned or acquired by the employing institution or any supervised or supervising institution as a result of foreclosure or similar action at any time during the agent's employment. The prohibition would apply for as long as the property is owned or acquired by the System institution, and for 12 months after the property is transferred out of the System institution or after the agency relationship is terminated, whichever occurs first.

M. Purchase of System Obligations [current § 612.2270 is
proposed § 612.2190]

We revised this section to clarify that directors and employees may not purchase any obligation of a System institution except as specifically stated.

III. Regulatory Flexibility Act

Pursuant to section 605(b) of the Regulatory Flexibility Act (5 U.S.C. 601 et seq.), the FCA hereby certifies that the proposed rule would not have a significant economic impact on a substantial number of small entities. Each of the banks in the Farm Credit System, considered together with its affiliated associations, has assets and annual income in excess of the amounts that would qualify them as small entities. Therefore, Farm Credit System institutions are not "small entities" as defined in the Regulatory Flexibility Act.

List of Subjects in 12 CFR Part 612

Agriculture, Banks, banking, Conflict of interests, Crime, Investigations, Rural areas.

For the reasons stated in the preamble, part 612 of chapter VI, title 12 of the Code of Federal Regulations is proposed to be amended as follows:

PART 612--STANDARDS OF CONDUCT AND REFERRAL OF KNOWN OR
SUSPECTED CRIMINAL VIOLATIONS

1. The authority citation for part 612 continues to read as follows:

Authority: Secs. 5.9, 5.17, 5.19 of the Farm Credit Act (12 U.S.C. 2243, 2252, 2254).

2. Subpart A, consisting of §§ 612.2130 through 612.2270, is revised to read as follows:

Subpart A--Standards of Conduct

Sec.

612.2130	Definitions.
612.2135	Responsibilities and conduct.
612.2136	Conflicts of interest.
612.2140	Director reporting.
612.2145	Directors--prohibited conduct.
612.2150	Employee reporting.
612.2155	Employees--prohibited conduct.
612.2157	Joint employees.
612.2160	Institution responsibilities.
612.2165	Code of ethics, policies, and procedures.
612.2170	Standards of Conduct Official.
612.2180	Standards of Conduct for agents.
612.2190	Purchase of System obligations.
612.2260	[Reserved]
612.2270	[Reserved]

Subpart A--Standards of Conduct

§ 612.2130 Definitions.

For purposes of this part, the following terms are defined:

Agent means any person, other than a director or employee, who currently represents a System institution in contacts with third parties or who currently provides

professional services to a System institution, such as legal, accounting, appraisal, and other similar services.

Code of Ethics means a written set of standards, rules, values, and guidance that is used to ensure the ethical conduct of those who sign it, and that reflects professionalism and discourages misconduct so that the best interests of the institution are advanced.

Conflicts of interest or the appearance thereof exists when a person has a financial interest in a transaction, relationship, or activity that actually affects or has the appearance of affecting the person's ability to perform official duties and responsibilities in a totally impartial manner and in the best interest of the employing institution when viewed from the perspective of a reasonable person with knowledge of the relevant facts.

Controlled entity and entity controlled by, for the purposes of this rule only, means an interest in an entity in which the individual, directly or indirectly, or acting through or in concert with one or more persons:

- (1) Owns 5 percent or more of the equity;
- (2) Owns, controls, or has the power to vote 5 percent or more of any class of voting securities; or
- (3) Has the power to exercise a controlling influence over the management of policies of such entity.

Employee means any salaried officer or part-time, full-time, temporary salaried employee or any non-salaried employee who receives a wage.

Entity means a corporation, company, association, firm, joint venture, partnership (general or limited), unincorporated business entity, society, joint stock company, trust (business or otherwise), fund or other organization or institution.

Family means an individual and spouse and anyone having the following relationship to either: parent, spouse, son, daughter, sibling, stepparent, stepson, stepdaughter, stepbrother, stepsister, half-brother, half-sister, uncle, aunt, nephew, niece, grandparent, grandson, granddaughter, and the spouses of the foregoing and anyone whose association or relationship with the director or employee is the equivalent of the foregoing.

Financial interest means an interest in an activity, transaction, property, or relationship with a person or an entity that involves receiving or providing something of monetary value or other present or deferred compensation.

Financially obligated with means having a joint legally enforceable obligation with, being financially obligated on behalf of (contingently or otherwise), having an enforceable legal obligation secured by property owned

by another, or owning property that secures an enforceable legal obligation of another.

Material, when applied to a financial interest or transaction or series of transactions, means that the interest or transaction or series of transactions is of such magnitude that a reasonable person with knowledge of the relevant facts would question the ability of the person who has the interest or is party to such transaction(s) to perform the person's official duties objectively and impartially and in the best interest of the institution and its statutory purpose.

Mineral interest means any interest in minerals, oil, or gas, including, but not limited to, any right derived directly or indirectly from a mineral, oil, or gas lease, deed, or royalty conveyance.

OFI means other financing institutions that have established an access relationship with a Farm Credit bank or an agricultural credit bank under section 1.7(b)(1)(B) of the Act.

Officer means the chief executive officer, president, chief operating officer, vice president, corporate secretary, treasurer, general counsel, chief financial officer, and chief credit officer of each System

institution, and any person not so designated who holds a similar position of authority.

Ordinary course of business, when applied to a transaction, means:

(1) A transaction that is usual and customary between or among persons who are in business together; or

(2) A transaction with a person who is in the business of offering the goods or services that are the subject of the transaction on terms that are not preferential. Preferential means that the transaction is not on the same terms as those prevailing at the same time for comparable transactions for other persons who are not directors, employees, or agents of a System institution.

Person means individual or entity.

Relative means any member of the family as defined in this section.

Service corporation means each service corporation chartered under the Act.

Signed, has the same meaning as set forth in § 620.1 of this chapter.

Standards of Conduct Official means the official designated under § 612.2170.

Supervised institution is a term which only applies within the context of a System bank or an employee of a

System bank and refers to each association supervised by that bank.

Supervising institution is a term that only applies within the context of an association or an employee of an association and refers to the bank that supervises that association.

System institution and institution mean any bank, association, or service corporation, chartered under the Act in the Farm Credit System, including the Farm Credit Banks, banks for cooperatives, agricultural credit banks, Federal land bank associations, agricultural credit associations, Federal land credit associations, production credit associations, and the Federal Farm Credit Banks Funding Corporation.

Unincorporated business entities (UBE) has the same meaning as set forth in § 611.1151 of this chapter.

§ 612.2135 Responsibilities and conduct.

(a) Directors and employees of all System institutions must maintain high standards of industry, honesty, integrity, impartiality, and conduct in order to ensure the proper performance of System business and continued public confidence in the System and each of its institutions. The avoidance of misconduct and conflicts of

interest is indispensable to the maintenance of these standards.

(b) To achieve these high standards of conduct, directors and employees must observe, to the best of their abilities, the letter and intent of all applicable local, state, and Federal laws and regulations and policy statements, instructions, procedures, and guidance of the Farm Credit Administration. System institutions must exercise diligence and good judgment in carrying out their duties, obligations, and responsibilities.

§ 612.2136 Conflicts of interest.

(a) Each director, employee, and agent of a System institution, and consultants who provide expert or professional services to the System institution, must:

- (1) Take measures to avoid conflicts of interest;
- (2) Disclose conflicts of interest in any matters, activities or transactions pending at the System institution, or in the case of consultants, experts or professionals, disclose conflicts of interest in the matter, activity, or transaction for which they are providing services, including financial or other personal or official interests that may present a conflict of interest or the appearance thereof, to the Standards of Conduct Official; and

(b) If a person subject to paragraph (a) of this section has a conflict of interest in a matter, transaction or activity subject to official action, or before the board of directors, then the person must:

(1) Disclose to the official or the board all material non-privileged information relevant to the consideration of the matter, activity or transaction, including:

(i) The existence, nature, and extent of the person's interests; and

(ii) The facts known to the person as to the matter, activity or transaction under consideration;

(2) Refrain from participating in the official action or board discussion of the matter, activity or transaction; and

(3) Not vote on the matter or transaction.

(c) The System institution must establish policies and procedures to enforce this section which may include procedures by which the Standards of Conduct Official may waive the recusal requirement upon his or her written determination that a conflict of interest does not exist or would not interfere with the person's ability to perform impartially and in the best interest of the System institution.

§ 612.2140 Director reporting.

(a) Annually, as of the institution's fiscal year end, and at such other times as may be required to comply with paragraph (c) of this section, each director must file a written and signed statement with the Standards of Conduct Official that fully reports:

(1) The names of any immediate family members as defined in § 620.1(e) of this chapter, or affiliated organizations, as defined in § 620.1(a) of this chapter, who had transactions with the institution at any time during the year;

(2) Any matter required to be disclosed by § 620.6(f) of this chapter; and

(3) Any additional information the institution may require to make the disclosures required by part 620 of this chapter.

(b) Each director must, at such intervals as the institution's board determines is necessary to effectively enforce this regulation and the institution's standards of conduct policy and Code of Ethics adopted pursuant to § 612.2165, file a written and signed statement with the Standards of Conduct Official that contains those disclosures required by the regulations and such policy. At a minimum, these disclosures must include:

(1) All material financial interests with directors, employees, agents or borrowers of the employing, supervised, and supervising institution;

(2) The name of any relative or any person residing in the director's household, any business partner, or any entity controlled by the director or such persons (alone or in concert) if the director knows or has reason to know that such individual or entity transacts business with the institution or any institution supervised by the director's institution; and

(3) The name and the nature of the business of any entity in which the director has a material financial interest or on whose board the director sits if the director knows or has reason to know that such entity transacts business with:

(i) The director's institution or any institution supervised by the director's institution; or

(ii) A borrower of the director's institution or any institution supervised by the director's institution.

(c) Any director who becomes or plans to become involved in any relationship, transaction, or activity that may violate the institutions' Code of Ethics or is required to be reported under this section or could constitute a conflict of interest, must promptly report in writing such

involvement or plan to become involved to the Standards of Conduct Official for a determination of whether the relationship, transaction, or activity is, in fact, a conflict of interest.

(d) Unless a disclosure as a director candidate under part 620 of this chapter has been made within the preceding 180 calendar days, a newly elected or appointed director must report matters required to be reported in paragraphs (a), (b), and (c) of this section to the Standards of Conduct Official within 30 calendar days after the election or appointment and thereafter must comply with the requirements of this section.

§ 612.2145 Directors--prohibited conduct.

(a) Prohibited conduct. Except as specifically provided under paragraph (b) of this section, a director of a System institution must not:

(1) Participate, directly or indirectly, in deliberations on, or the determination of, any matter affecting, directly or indirectly, the financial interest of the director, any relative of the director, any person residing in the director's household, any business partner of the director, or any entity controlled by the director or such persons (alone or in concert);

(2) Divulge or make use of any fact, information, or document not generally available to the public that is acquired by virtue of serving on the board of a System institution;

(3) Use the director's position to obtain or attempt to obtain special advantage or favoritism for the director, any relative of the director, any person residing in the director's household, any business partner of the director, any entity controlled by the director or such persons (alone or in concert), any other System institution, or any person transacting business with the institution, including borrowers and loan applicants;

(4) Use the director's position or information acquired in connection with the director's position to solicit or obtain, directly or indirectly, any gift, fee, or other present or deferred compensation or for any other personal benefit on behalf of the director, any relative of the director, any person residing in the director's household, any business partner of the director, any entity controlled by the director or such persons (alone or in concert), any other System institution, or any person transacting business with the institution, including borrowers and loan applicants;

(5) Accept or solicit, directly or indirectly, any gift, fee, or other present or deferred compensation that is offered or could reasonably be viewed as being offered to influence official action or to obtain information that the director has access to by reason of serving on the board of a System institution;

(6) Knowingly acquire, directly or indirectly, any interest in any real or personal property, including mineral interests, that was owned or acquired by the employing, supervising, or any supervised institution as a result of foreclosure or similar action;

(7) Directly or indirectly borrow from, lend to, or become financially obligated with or on behalf of, a director, employee, or agent of the employing, supervising or supervised institution or a borrower, or loan applicant of the employing institution; or

(8) Violate an institution's policies and procedures governing standards of conduct or Code of Ethics.

(b) Exceptions to prohibited conduct. (1) A director may participate in deliberations and determinations of matters prohibited under paragraph (a) (1) of this section only if the matter is one of general applicability affecting all shareholders/borrowers in a

nondiscriminatory way, as determined by the Standards of Conduct Official.

(2) A director may divulge or make use of any fact, information, or document prohibited under paragraph (a)(2) of this section, only if in the performance of the director's official duties.

(3) A director may acquire an interest in any real or personal property prohibited under paragraph (a)(6) of this section only if the director did not participate in the deliberations or decision to foreclose, or take similar action, or to dispose of the property or in establishing the terms of the sale; and

(i) The director acquired the property through inheritance; or

(ii) The System institution did not own the property or interest at any time during the 12-month period before the director's acquisition of the property; or

(iii) The director acquired the property through public auction with open competitive bidding and the Standards of Conduct Official determined in writing, before the director acquired the property, that the director does not have an advantage over other bidders as a result of the director's position and that no other conflict of interest or appearance thereof exists.

(4) A director may enter into a lending transaction prohibited under paragraph (a)(7) of this section only if:

(i) The transaction is with a relative or any person residing in the director's household;

(ii) The transaction is undertaken in an official capacity in connection with the institution's discounting, lending or participation relationships with OFIs and other lenders; or

(iii) The Standards of Conduct Official, on a case-by-case basis, determines and documents, pursuant to a board adopted policy and in the manner outlined herein, that the potential for conflict is insignificant. The Standards of Conduct Official's determination must:

(A) Be in writing;

(B) Adequately demonstrate that the transaction is in the ordinary course of business or is not material in amount or value;

(C) Adequately demonstrate that the director did not participate in the determination of any matter affecting the financial interests of the other party to the transaction except those matters affecting all shareholders/borrowers in a nondiscriminatory way;

(D) Be made before the director enters into the transaction, or at the time the director is appointed or elected; and

(E) Be renewed annually, as applicable.

§ 612.2150 Employee reporting.

(a) Annually, as of the institution's fiscal yearend, and at such other times as may be required to comply with paragraph (c) of this section, each senior officer as defined in § 619.9310 of this chapter must file a written and signed statement with the Standards of Conduct Official that fully reports:

(1) The names of any immediate family members, as defined in § 620.1(e) of this chapter, or affiliated organizations, as defined in § 620.1(a) of this chapter, who had transactions with the institution at any time during the year;

(2) Any matter required to be disclosed by § 620.6(f) of this chapter; and

(3) Any additional information the institution may require to make the disclosures required by part 620 of this chapter.

(b) Each employee must, at such intervals as the institution's board determines is necessary to effectively enforce this regulation and the institution's standards of

conduct policy and Code of Ethics adopted pursuant to § 612.2165, file a written and signed statement with the Standards of Conduct Official that contains those disclosures required by the regulation and such policy. At a minimum, these disclosures must include:

(1) All material financial interests with directors, employees, agents or borrowers of the employing, supervised, and supervising institutions;

(2) The name of any relative or any person residing in the employee's household, any business partner, or any entity controlled by the employee or such persons (alone or in concert) if the employee knows or has reason to know that such individual or entity transacts business with the employing institution, or any institution supervised by the employing institution; and

(3) The name and the nature of the business of any entity in which the employee has a material financial interest or on whose board the employee sits if the employee knows or has reason to know that such entity transacts business with:

(i) The employing institution or any institution supervised by the employing institution; or

(ii) A borrower of the employing institution or any institution supervised by the employing institution.

(c) Any employee who becomes or plans to become involved in any relationship, transaction, or activity that is required to be reported under this section or could constitute a conflict of interest must promptly report in writing such involvement to the Standards of Conduct Official for a determination of whether the relationship, transaction, or activity is, in fact, a conflict of interest.

(d) A newly hired employee must report matters required to be reported in paragraphs (a), (b), and (c) of this section to the Standards of Conduct Official five (5) business days after starting employment and thereafter must comply with the requirements of this part.

§ 612.2155 Employees--prohibited conduct.

(a) Prohibited conduct. Except as specifically provided under paragraph (b) of this section, an employee of a System institution must not:

(1) Participate, directly or indirectly, in deliberations on, or the determination of, any matter affecting, directly or indirectly, the financial interest of the employee, any relative of the employee, any person residing in the employee's household, any business partner of the employee, or any entity controlled by the employee or such persons (alone or in concert);

(2) Divulge or make use of any fact, information, or document not generally available to the public that is acquired by virtue of being an employee of a System institution;

(3) Use the employee's position to obtain or attempt to obtain special advantage or favoritism for the employee, any relative of the employee, any person residing in the employee's household, any business partner of the employee, any entity controlled by the employee or such persons (alone or in concert), any other System institution, or any person transacting business with the institution, including borrowers and loan applicants;

(4) Serve as an officer or director of an entity other than a System institution that transacts business with a System institution in the district or of any commercial bank, savings and loan, or other non-System financial institution. For the purposes of this paragraph, "transacts business" does not include loans by a System institution to a family-owned entity, service on the board of directors of the Federal Agricultural Mortgage Corporation, or transactions with nonprofit entities or entities in which the System institution has an ownership interest;

(5) Use the employee's position or information acquired in connection with the employee's position to solicit or obtain, directly or indirectly, any gift, fee, or other present or deferred compensation or for any other personal benefit on behalf of the employee, any relative of the employee, any person residing in the employee's household, any business partner of the employee, any entity controlled by the employee or such persons (alone or in concert), any other System institution, or any person transacting business with the institution, including borrowers and loan applicants;

(6) Accept or solicit, directly or indirectly, any gift, fee, or other present or deferred compensation that is offered or could reasonably be viewed as being offered to influence official action or to obtain information that the employee has access to by reason of employment with a System institution;

(7) Knowingly acquire, directly or indirectly, any interest in any real or personal property, including mineral interests, that was owned or acquired by the employing, supervising, or any supervised institution as a result of foreclosure or similar action;

(8) Directly or indirectly borrow from, lend to, or become financially obligated with or on behalf of, a

director, employee, or agent of the employing, supervising, or supervised institution or a borrower or loan applicant of the employing institution;

(9) Act as a real estate agent or broker;

(10) Act as an agent or broker in connection with the sale and placement of insurance; or

(11) Violate an institution's policies and procedures governing standards of conduct or Code of Ethics.

(b) Exceptions to prohibited conduct. (1) An employee may participate in deliberations and determinations of matters prohibited under paragraph (a) (1) of this section only if the matter is one of general applicability affecting all shareholders/borrowers in a nondiscriminatory way, as determined by the Standards of Conduct Official.

(2) An employee may divulge or make use of a fact, information, or document prohibited under paragraph (a) (2) of this section only if in the performance of official duties.

(3) Notwithstanding the prohibitions in paragraph (a) (4) of this section, an employee may serve as an officer or director of an employee credit union. With the prior approval of the board of the employing institution, an employee of a Farm Credit Bank or association may serve as

a director of a cooperative that borrows from an agricultural credit bank. Prior to approving an employee's request, the board must determine whether the employee's proposed service as a director is likely to cause the employee to violate any regulations in this part or the institution's policies, e.g., the requirements relating to devotion of time to official duties.

(4) An employee may acquire an interest in real or personal property prohibited under paragraph (a)(7) of this section only if the employee did not participate in the deliberations or decision to foreclose on the property or to take action, or to dispose of the property or in establishing the terms of the sale; and

(i) The employee acquired the property through inheritance; or

(ii) The System institution did not own the property or interest at any time during the 12-month period before the employee's acquisition of the property.

(5) An employee may enter into a lending transaction prohibited under paragraph (a)(8) of this section only if:

(i) The transaction is with a relative or any person residing in the employee's household;

(ii) The transaction is undertaken in an official capacity in connection with the institution's discounting,

lending, or participation relationships with OFIs and other lenders; or

(iii) The Standards of Conduct Official on a case-by-case basis, determines and documents, pursuant to a board adopted policy under § 612.2165 and in the manner outlined herein, that the potential for conflict is insignificant.

The Standards of Conduct Official's determination must:

(A) Be in writing;

(B) Adequately demonstrate that the transaction is in the ordinary course of business or is not material in value or amount;

(C) Adequately demonstrate that the employee did not participate in the determination of any matter affecting the financial interests of the other party to the transaction except those matters affecting all shareholders/borrowers in a nondiscriminatory way;

(D) Be made before the transaction in question is entered into; and

(E) Be renewed annually, as applicable.

(6) Paragraph (a)(9) of this section does not apply to transactions involving the purchase or sale of real estate intended for the use of the employee, a member of the employee's family, or a person residing in the employee's household.

(7) Paragraph (a)(10) of this section does not apply to the sale or placement of insurance authorized by section 4.29 of the Act.

§ 612.2157 Joint employees.

(a) An employee of a Farm Credit bank may serve as an employee of an association in its district only if:

(1) The employee is not an officer of the Farm Credit bank and will not serve as an officer of the association;
or

(2) Before such service begins, the Farm Credit bank's Standards of Conduct Official consents in writing to such service, the Farm Credit bank board of directors agrees that the interest of both System institutions outweighs the potential for conflicts of interest or conflicts related to devotion of time to official duties, the Farm Credit bank delivers written notice to the Farm Credit Administration, and the Farm Credit Administration does not object to such service within ten (10) calendar days of receiving the notice.

(b) Each institution must appropriately reflect the expense of joint employees in its financial statements.

§ 612.2160 Institution responsibilities.

Each institution must:

(a) Ensure compliance with this part by its directors, employees, and agents and at a minimum:

(1) Provide support as necessary to the Standards of Conduct program including assigning appropriate resources and staffing to the Standards of Conduct Official;

(2) Act promptly to preserve the integrity of and public confidence in the institution in any matter involving a conflict of interest or the appearance of a conflict of interest, whether or not specifically addressed by this subpart or the policies and procedures adopted pursuant to § 612.2165; and

(3) Notify the Farm Credit Administration immediately of known or suspected material standards of conduct violations as described in § 612.2170(b)(7).

(b) Take appropriate measures to ensure that all directors and employees are informed of the requirements of this regulation and policies and procedures adopted pursuant to § 612.2165.

(c) Maintain all standards of conduct policies and procedures, reports, investigations, determinations, and evidence of compliance with this part for a minimum of six (6) years.

(d) Remain informed of applicable industry approved best practices for standards of conduct.

(e) Ensure that directors and employees annually certify in writing that they will adhere to the institution's standards of conduct policy and Code of Ethics.

(f) Provide its agents a copy of the institution's standards of conduct policy and Code of Ethics;

(1) Adequately document which of its agents are subject to industry or professional ethics standards; and

(2) Require each agent that is not subject to industry or professional ethics standards to certify that he or she will adhere to the provisions of the institution's Code of Ethics applicable to agents.

(g) Ensure that compliance with the standards of conduct program is a component of the institution's risk assessment process subject to periodic audit by a person or entity independent of the program.

(h) Develop, implement and maintain an effective method of internal controls over the reporting, disclosure and other requirements of this part. The method of internal controls, at a minimum, must comply with the requirements of applicable Farm Credit Administration regulations, including § 618.8430 of this chapter and include controls for:

(1) The confidentiality of information reported to and maintained by the Standards of Conduct Official; and

(2) The audit of the standards of conduct program for compliance by a person or entity independent of the program.

§ 612.2165 Code of Ethics, policies, and procedures.

(a) Each institution's board of directors must adopt:

(1) Policies and procedures governing standards of conduct for directors, employees, and agents; and

(2) A code of Ethics that applies to directors and employees and that includes a provision for the ethical conduct of agents to ensure the avoidance of conflicts of interest in the performance of their duties. The Code of Ethics must include specific guidelines on what is acceptable and unacceptable conduct. The Code of Ethics must be signed by directors and employees. Agents must be presented with the institution's Code of Ethics, and agents not subject to industry or professional ethics standards must sign the institution's Code of Ethics provisions applicable to agents. The institution's Code of Ethics must:

(i) Promote honest and ethical conduct, including the ethical handling of actual or apparent conflicts of interest;

(ii) Promote integrity and compliance with applicable laws, rules and regulations governing standards of conduct;

(iii) Inform directors and employees that they will be held accountable for adhering to the institution's Code of Ethics, or in the case of agents, to industry or professional ethics standards or, in the absence thereof, to the System institution's Code of Ethics provisions applicable to agents;

(iv) Prohibit conduct involving dishonesty, fraud, or deceit and discourage the commitment of any act that reflects adversely on the reputation, integrity, or competency of the System institution or the System;

(v) Prohibit conduct involving misuse of office; and

(vi) Provide for the prompt reporting to the Standards of Conduct Official any person or persons in violation of the institution's Code of Ethics and of any activity that may require further investigation and reporting under § 612.2301;

(3) Policies and procedures related to UBEs that ensure the System institution's directors, employees, and agents and the UBE members, partners, employees and agents comply with their employing institution's standards of conduct and avoid conflicts of interest in carrying out their duties with respect to the UBE.

(b) Board policies and procedures adopted pursuant to paragraph (a) of this section must reflect due consideration of the potential adverse impact of activities permitted under the policies and procedures and must at a minimum:

(1) Establish requirements and prohibitions as are necessary to promote public confidence in the institution and the System, preserve the integrity and independence of the supervisory process, and prevent the improper use of official property, position, or information. In developing such requirements and prohibitions, the institution must address such issues as the hiring of relatives, political activity, devotion of time to duty, use of institution resources, the exchange of gifts and favors among directors and employees of the employing, supervising, and supervised institution, and the circumstances under which gifts may be accepted by directors and employees from outside sources, in light of the foregoing objectives;

(2) Outline authorities and responsibilities of the Standards of Conduct Official, including:

(i) The authority and responsibility to review for compliance with this subpart all loans before the supervisory bank's approval under §§ 614.4460 and 614.4470, respectively; and

(ii) A process to allow the Standards of Conduct Official to report matters to the board without fear of reprisal;

(3) Establish criteria for business relationships and transactions not specifically prohibited by this part between employees or directors and borrowers, loan applicants, directors, or employees of the employing, supervised, or supervising institutions, or persons transacting business with such institutions, including OFIs or other lenders having an access or participation relationship;

(4) Establish criteria under which employees may accept outside employment or compensation;

(5) Establish conditions under which employees may receive loans from System institutions;

(6) Establish conditions under which employees may acquire an interest in real or personal property that served as collateral for a loan from a System institution;

(7) Establish conditions under which employees may purchase any real or personal property of a System institution acquired by such institution for its operations. System institutions must use open competitive bidding whenever they sell surplus property above a stated value (as established by the board) to their employees;

(8) Provide for a reasonable period of time for directors and employees to terminate transactions, relationships, or activities that are subject to prohibitions that arise at the time of adoption or amendment of the policies;

(9) Require new directors and new employees involved in transactions, relationships, and activities prohibited by these regulations or internal policies to terminate such transactions within the same time period established for existing directors or employees pursuant to paragraph (b)(8) of this section, beginning with the commencement of the director's term for new directors, and commencement of official duties for new employees, or such shorter time period as the institution may establish;

(10) Establish procedures providing for a director's, employee's, or agent's recusal from official action on any matter in which the director, employee, or agent is prohibited from participating under these regulations or the institution's policies;

(11) Establish documentation requirements demonstrating compliance with standards of conduct decisions and board policy;

(12) Establish reporting requirements, consistent with this part, to enable the institution to comply with

§ 620.6 of this chapter, monitor conflicts of interest, and monitor recusal compliance;

(13) Establish appeal procedures available to any employee to whom any required approval has been denied;

(14) Prohibit directors and employees from purchasing or retiring any preferred stock of the institution in advance of the release of material non-public information concerning the institution to other stockholders;

(15) Establish when directors and employees may purchase and retire their preferred stock in the institution;

(16) Require annual training and other appropriate measures to ensure that all directors and employees are educated on best practices for ethical behavior and standards of conduct and perform their duties and responsibilities in an objective and impartial manner; and

(17) Require that the institution report to the Farm Credit Administration exceptions authorized by the board pursuant to paragraph (c) of this section.

(c) Board policies and procedures adopted pursuant to paragraphs (a) and (b) of this section may provide for:

(1) The board to consider a case-by-case exception to conflicts of interest requirements (§ 612.2136), director and employee reporting requirements (§§ 612.2140 and

612.2150), the 5-percent threshold on controlled entity (§ 612.2130), joint employee prohibitions (§ 612.2157), employee prohibitions on serving as an officer or director of a non-System financial institution (§ 612.2155(a)(4)), and director and employee prohibitions on sharing information (§§ 612.2145(a)(2) and 612.2155(a)(2), respectively). An exception may be authorized only upon board approval after the board considers the written recommendation of the Standards of Conduct Official. The recommendation must be adequately supported by the Standards of Conduct Official's written determination that in that particular matter or transaction application of the prohibition subject to the exception is not necessary to avoid a conflict of interest, to avoid the appearance of a conflict of interest or to ensure the confidence in the impartiality and objectivity of the director, employee, or System institution. The board must provide for periodic review of the criteria to determine whether the exception continues to be appropriate. If the board approves an exception, it may impose appropriate conditions, such as requiring a written disqualification or additional public disclosure.

(2) Exceptions to reporting requirements under §§ 612.2140 and 612.2150 and exceptions to the requirements

under §§ 612.2145(b)(4) and 612.2155(b)(6) that the Standards of Conduct Official review a lending transaction before it is entered into. Broad based exceptions in policies may be authorized only if the potential for conflict of interest in that category of interests or transactions is insignificant. The potential for conflict of interest may only be considered insignificant if:

(i) The board determines, under its policies and procedures, that the type of interest or transaction is so immaterial in amount or value that no reasonable person with knowledge of all the facts could conclude that the interest or transaction would influence a director's or employee's ability to act impartially and in the best interests of the System institution. For this exception, transactions otherwise prohibited under §§ 612.2145 and 612.2155 do not require the prior approval of the Standards of Conduct Official or reporting under §§ 612.2140 and 612.2150; or

(ii) The board determines, under its policies and procedures that the types of interests or transactions covered by the exception or reporting requirement are in the ordinary course of business. For this exception, transactions otherwise prohibited under §§ 612.2145 and 612.2155 do not require the prior approval of the Standards

of Conduct Official but must be reported under §§ 612.2140 and 612.2150, and must be reviewed by the Standards of Conduct Official at least annually; and

(iii) The board must consider the written recommendation of the Standards of Conduct Official in developing these policy exceptions. The recommendation must be adequately supported by the Standards of Conduct Official's written determination that the amount of value in the transaction or the particular type of interest or transaction, does not require application of the reporting requirement or prohibition subject to the exception and is not necessary to avoid a conflict of interest, to avoid the appearance of a conflict of interest or to ensure the confidence in the impartiality and objectivity of the director, employee, or System institution.

(d) An institution's directors and employees, including the Standards of Conduct Official, must not engage in any act or practice to evade the prohibitions and other requirements of this part.

(e) The Farm Credit Administration may take appropriate action against any institution, director or employee who or that has entered into any transaction for the purpose of evading the requirements of this part.

(f) Notwithstanding the exceptions that may be authorized and approved under this subpart, the Farm Credit Administration may find that a particular financial interest or transaction, relationship, or activity constitutes a conflict of interest or the appearance of a conflict of interest.

§ 612.2170 Standards of Conduct Official.

(a) Each institution's board of directors must:

(1) Designate an officer of the institution as its Standards of Conduct Official; and

(2) Authorize other employees of the institution or outside counsel or consultants to assist the Standards of Conduct Official as needed, and dedicate resources as needed, to ensure the effective operations of the institution's standards of conduct program for compliance with institution policies and the Farm Credit Administration's standards of conduct regulations.

(b) The Standards of Conduct Official must:

(1) Advise directors, director candidates, employees, and potential new employees concerning the provisions of this part;

(2) Receive, review, and maintain reports required by this part;

(3) Make such determinations as are required by this part;

(4) Maintain records of determinations as are required by this part;

(5) Make appropriate investigations, as directed by the institution's board;

(6) Report to the board no less than annually on the effectiveness of the institution's standards of conduct policy and its implementation;

(7) Report promptly to the institution's board and the Office of General Counsel, Farm Credit Administration, all cases where:

(i) A preliminary investigation indicates that a Federal criminal statute pursuant to subpart B of this part may have been violated;

(ii) An investigation results in the resignation or discharge of an employee or the resignation or potential removal of a director; or

(iii) A known or suspected criminal or standards of conduct violation by a director, employee or agent may have an adverse impact on continued public confidence in the System or any of its institutions.

(8) Investigate or cause to be investigated all cases involving:

(i) Possible violations of criminal statutes by a director, employee or agent;

(ii) Possible violations of §§ 612.2136, 612.2145 and 612.2155, and applicable policies and procedures approved under § 612.2165;

(iii) Complaints received against the directors, employees, and agents of such institution; and

(iv) Possible violations of other provisions of this part or when the activities or suspected activities of a director, employee or agent are of a sensitive nature and could affect continued public confidence in the institution or System.

(c) A Farm Credit bank may provide assistance to an affiliated association's board of directors and Standards of Conduct Official in complying with this part.

(d) A System institution may use an outside counsel or consultant to assist in complying with this part. However, the Standards of Conduct Official must oversee the outside counsel or consultant and remains accountable to the board.

(e) The Standards of Conduct Official must coordinate with the board and management in administering annual training to ensure that directors and employees remain

informed of the institution's current standards of conduct policy and Code of Ethics.

§ 612.2180 Standards of conduct for agents.

(a) Agents of System institutions must maintain high standards of honesty, integrity, and impartiality in order to ensure the proper performance of System business and continued public confidence in the System and its institutions. The avoidance of misconduct and conflicts of interest is indispensable to the maintenance of these standards.

(b) System institutions must utilize safe and sound business practices in the engagement, utilization, and retention of agents. These practices must provide for the selection of qualified and reputable agents. Agents representing a System institution in contacts with third parties or who provide consultant or professional services such as legal, accounting and appraisal, must review and acknowledge receipt of the institution's Code of Ethics. Agents must certify to the System institution that the agent will adhere to the agent's professional or industry ethics standards, or to the institution's Code of Ethics provisions applicable to agents. Employing System institutions are responsible for the actions of their agents, and must take appropriate investigative and

corrective action in the case of a breach of fiduciary duties by the agent or failure of the agent to carry out its duties.

(c) System institutions must exercise special diligence and control, through good business practices, to avoid or control situations that have inherent potential for sensitivity, either real or perceived. These areas include the employment of agents who are related to directors or employees of System institutions; the solicitation and acceptance of gifts, contributions, or special considerations by agents; and the use of System and borrower information obtained in the course of the agent's association with System institutions.

(d) An agent may not knowingly acquire, directly or indirectly, except through inheritance, any interest in real or personal property, including a mineral interest, that was owned by the employing institution or any supervised or supervising institution as a result of foreclosure or similar action during the agent's employment. This prohibition applies for one (1) year after the transfer of the property out of the System institution or after the termination of the agent relationship, whichever occurs first.

§ 612.2190 Purchase of System obligations.

(a) Employees and directors of System institutions must not purchase any obligation of a System institution, including any joint, consolidated, or Systemwide obligation, unless such obligation is:

(1) Part of an offering available to the general public; and

(2) Purchased through a dealer or dealer bank affiliated with a member of the selling group designated by the Federal Farm Credit Banks Funding Corporation or purchased in the secondary market.

(b) A director or employee of the Federal Farm Credit Banks Funding Corporation must not purchase or otherwise acquire, directly or indirectly, except by inheritance, any obligation of a System institution, including any joint, consolidated, or Systemwide obligation.

§§ 612.2260 and 612.2270 [Reserved]

Dated: February 7, 2014.

Dale L. Aultman,
Secretary,
Farm Credit Administration Board.

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